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Before the

FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of **Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers**	**CC Docket No. 95-185**

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COMMENTS OF TIME WARNER COMMUNICATIONS HOLDINGS, INC.

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SUMMARY

TW Comm supports the Commission's effort to establish rates for CMRS-LEC interconnection that encourage the development of the mobile telecommunications industry as a substitute to traditional landline local exchange service. TW Comm also concurs with the Commission that the FCC should recognize and account for the unequal bargaining position of new entrants relative to incumbent carriers as it establishes rates, terms, and conditions for mutual compensation and other interconnection elements.

The Telecommunications Act of 1996 charges the Commission with complex, significant rulemakings that will require the Commission's immediate and in-depth attention during the upcoming months. Furthermore, the Commission may establish policies and principles in these proceedings that should inform any final decisions in this rulemaking. For these reasons, TW Comm recommends that the FCC seek a fair but expedient interim resolution to the outstanding matters under investigation in this NPRM - one that enables the CMRS industry to continue to evolve, but one that is not administratively burdensome - so that the FCC can devote its limited resources to the more pressing national telecommunications matters that have been identified by the Act.

In these comments, TW Comm demonstrates that Ramsey pricing and the so-called efficient component pricing rule should be rejected as irrelevant and anticompetitive foundations for establishing rates for monopoly network elements. The mispricing of network termination and interconnection elements that are

essential for potential competitors to successfully enter the local market will thwart the Commission's goals of promoting competition and economic development. Instead, in those limited instances where bill and keep is inappropriate, the FCC should base rates on long run incremental costs and not on embedded costs.

As the FCC has tentatively concluded, however, bill and keep is the most appropriate interim model for mutual compensation between LECs and CMRS providers for several reasons: (1) incumbent LECs have apparently failed to comply with the FCC's directives regarding mutual compensation; (2) the market power of the incumbent LECs means that any delay in implementing a pricing model benefits the incumbent at the expense of the new entrant; and (3) bill and keep as well as changing market conditions may cause CMRS-LEC traffic to become more in balance.

Although bill and keep is an appropriate interim measure for CMRS-LEC mutual compensation, it is not necessarily an appropriate long-term model. The future applicability of bill and keep depends upon whether CMRS providers assume the obligations that LECs and CLECs fulfill, and also on the balance of traffic that is actually exchanged between CMRS and LEC networks.

Section 332 of the Communications Act clearly reflects an intent by Congress to foster the development of nationwide wireless networks. When considering CMRS interconnection arrangements generally, and in particular when considering the compensation principles for those arrangements, preemption is necessary to implement policies deemed essential to the national interest. The Telecommunications Act of 1996 provides further support for an interpretation that preempts state regulation in this area.

Finally, the mutual compensation model that the FCC adopts in this proceeding should apply only to those segments of the CMRS industry where there is a clear potential for two-way telecommunications services.

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In the Matter of **Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers**	**CC Docket No. 95-185**

Time Warner Communications Holdings, Inc.[1] ("TW Comm") hereby submits its comments in the above-captioned proceeding.[2]

I. General Comments and Introduction

TW Comm fully supports the Federal Communications Commission's ("FCC" or "Commission") endeavor to establish rates for interconnection between commercial mobile radio service ("CMRS") providers and local exchange carriers ("LEC") that promote economic development, competition, and the efficient pricing of bottleneck network elements.[3] The Commission has also appropriately expanded its rulemaking in order to seek comment on the implications of the Telecommunications Act of

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1 Time Warner Communications Holdings, Inc. is a wholly-owned subsidiary of the Time Warner Entertainment Company, L.P. ("Time Warner Entertainment"). TW Comm is distinguished from Time Warner Telecommunications, a Division of Time Warner Entertainment that submitted comments in earlier dockets on related issues.

2 In re Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers, Notice of Proposed Rulemaking, CC Docket No. 95-185, FCC 95-185 (January 11, 1996 (hereinafter "NPRM").

3 See e.g., NPRM at paras. 5-7, 10; In re Implementation of Sections 3(n) and 332 of the Communications Act Regulatory Treatment of Mobile Services, Second Report and Order, 9 FCC Rcd 1411 (1994) (hereinafter "CMRS Second Report").

1996[4] (the "1996 Act") for such interconnection issues, particularly with regard to jurisdiction as noted in paragraphs 96 through 114 of the NPRM.[5]

The 1996 Act charges the Commission with numerous, significant, and complex rulemakings that the FCC must pursue during the upcoming months. Congress did not, however, establish mutual compensation between CMRS providers and LECs as one of the priorities for national telecommunications policy. In light of that omission, the FCC should seek a fair but expedient interim resolution to these issues, supporting the efficient evolution of the CMRS industry without being administratively cumbersome and without compromising the ultimate policy determinations that the 1996 Act requires. After the Commission has completed the many rulemakings associated with the 1996 Act's implementation, it can then establish long-term CMRS-LEC mutual compensation policies, applying the policies established in those rulemakings.

Some of the implications of the 1996 Act for this rulemaking are discussed in greater detail below; however, at the outset, it is useful to note the silence of the 1996 Act with regard to the possibility that CMRS providers might be competitive LECs. Congress did not explicitly include CMRS providers in the 1996

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[4] Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996) (hereinafter "1996 Act").

[5] See In re Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers, Order and Supplemental Notice of Proposed Rulemaking, CC Docket No. 95-186, FCC 96-61, para. 6 (February 16, 1996). The FCC also observes that "sections 251 through 253 of the Telecommunications Act of 1996 may impact the proposals in the Notice." Id. n.3.

Act's definition of local exchange carriers, but rather afforded the Commission substantial discretion to apply the LEC-specific portions of the 1996 Act to CMRS providers as circumstances may warrant.[6]

As a general matter, the 1996 Act distinguishes among (and establishes varying levels of obligations and requirements for) (1) incumbent local exchange carriers, (2) local exchange carriers, and (3) telecommunications carriers, with the first group being a subset of the latter two categories, and the second group being a subset of the third category.[7] CMRS providers are telecommunications carriers but until such time as the Commission finds otherwise, CMRS providers are neither incumbent local exchange carriers nor local exchange carriers.

In a decision issued in March 1994, the Commission required local exchange carriers[8] to offer interconnection to CMRS providers on reasonable terms and conditions and under the principle of mutual compensation.[9] However, it appears that LECs have not been complying with the requirement to participate in mutual compensation arrangements with CMRS providers.[10] For this and other reasons, the FCC seeks comments on establishing

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6 1996 Act at Sec. 3 (to be codifed at 47 U.S.C. 153 (a)(44)).

7 Id. at Sec. 3(a)(2)(44); Sec. 3(a)(2)(49); Sec. 251(h).

8 It is not readily obvious whether the FCC intended this requirement to apply to competitive LECs.

9 See CMRS Second Report at para. 230.

10 NPRM at para. 81.

rates for interconnection between CMRS and LEC networks that can be readily adopted. The Commission also seeks comments on long-term policies and prices, including the degree of preemption that the Commission should exercise with regard to state decisionmaking about CMRS-LEC interconnection rates.[11]

The FCC's specific purpose for this proceeding is to focus on the compensation arrangements for interconnection between LECs and CMRS providers,[12] and its broader purpose is to "encourage the development of CMRS, especially in competition with LEC-provided wireline service."[13] The FCC also acknowledges the possible relevance of decisions rendered in this proceeding to other matters such as the upcoming access reform proceeding.[14]

TW Comm concurs with the Commission that "it is important that the prices, terms, and conditions of interconnection arrangements not serve to buttress LEC market power against erosion by competition"[15] and, indeed, this statement is fully consistent with the position taken by TW Comm in numerous state proceedings on local competition. The prices that are set for

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[11] The FCC states that contrary to its conclusion in earlier orders, "preemption under Louisiana PSC may well be warranted here on the basis of inseverability, particularly in light of the strong federal policy underlying Section 332 favoring a nationwide wireless network." NPRM at para. 111 (footnote omitted).

[12] NPRM at para. 15.

[13] Id. at para. 2.

[14] Id. at para. 17.

[15] Id. at para. 2.

CMRS interconnection will directly and substantially influence the development of CMRS as an alternative to incumbent local exchange carriers. Moreover, the FCC raises several legitimate concerns about the unequal bargaining position that incumbent LECs enjoy with regard to other carriers seeking interconnection.[16] These concerns are particularly valid in an industry under transition to competition and for one in which incumbent local exchange carriers control network elements that are essential to the successful entry by potential competitors.

Furthermore, TW Comm supports the Commission's effort to encourage competition in the local market through a wide variety of technologies. It is important, however, to recognize that different segments of the telecommunications industry are at different stages of progress in offering a comparable substitute to the basic exchange services of incumbent local exchange carriers. Accordingly, it is essential that CMRS interconnection be established pursuant to a consistent set of fundamental pricing principles applicable to the broad range of potential LEC competitors.

In these comments, TW Comm will address (1) existing compensation arrangements; (2) the various pricing principles that the Commission describes; (3) interim and long-term options for setting CMRS-LEC interconnection rates; (4) jurisdiction over CMRS-LEC interconnection; and (5) the application of mutual compensation to the various CMRS services.

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[16] Id. at para. 12.

II. Compensation for Interconnected Traffic between LEC and CMRS Provider Networks

A. Compensation Arrangements

Changing market conditions may eventually justify "bill and keep" as a long-term pricing model for LEC-CMRS interconnections if traffic flows change and CMRS providers assume the obligations of co-carriers. Several reasons support adoption of bill and keep for CMRS-LEC interconnection as an interim measure: (1) Incumbent LECs apparently have failed to comply with the FCC's directives regarding mutual compensation; (2) the unequal bargaining positions of the incumbent LECs and CMRS providers mean that it is essential to implement a mechanism that can be readily adopted to prevent further anticompetitive foot-dragging by incumbent carriers; (3) the form of mutual compensation adopted by the FCC and changing market conditions may influence the flow of traffic between CMRS and incumbent LEC networks, i.e., a bill and keep approach may cause traffic to become more in balance; and (4) bill and keep causes no administrative burdens and avoids the costly establishment of traffic measurement and billing systems for an interim period. Therefore, bill and keep should be adopted as an interim measure in order to equalize the lopsided bargaining power of incumbent LECs relative to CMRS providers expeditiously and to provide an opportunity to determine whether bill and keep and changing market conditions will affect the traffic imbalance that exists today between mobile and landline networks. During this interim period, the FCC should investigate, identify and adopt a long-term approach to pricing mutual compensation for those situations where traffic is not approximately in balance or where providers are not co-carriers. This section describes the pricing principles that should guide that effort and also provides specific recommendations for pricing models.

1. Existing Compensation Arrangements

The NPRM states that cellular carriers presently pay LECs three types of usage-sensitive charges for local calls originated by cellular subscribers to incumbent LEC subscribers: (1) per-call charges for call set-up; (2) per-minute charges for usage; and (3) per-minute, per-mile charges for transport between the cellular carrier's mobile telephone switching office ("MTSO") and the LEC's tandem or end-office switch.[17] In addition, cellular carriers have contended that, contrary to the FCC's intent, cellular carriers are being forced to pay LECs for calls that originate with LEC customers and terminate to cellular customers.[18] The NPRM seeks additional information about existing LEC-CMRS interconnection arrangements, and the extent to which the Commission's mutual compensation requirement is not being followed.[19]

The implication is that incumbent LECs are failing to comply with the FCC's requirement for mutual compensation[20] which, if

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[17] Id. at para. 40.

[18] Id.

[19] Id. at para. 41.

[20] Id. at para. 81.

true, should be viewed seriously.[21] Such foot-dragging on the part of incumbent LECs underscores the importance of identifying an approach to pricing mutual compensation that can be expeditiously implemented. Otherwise, the unequal bargaining positions of CMRS providers and incumbent LECs will promote LEC rearguard protectionism at the expense of this newer segment of the industry. Thus, an immediate measure should be adopted in this proceeding while the FCC deliberates on the appropriate design of long-term pricing models.

As stated in the NPRM, CMRS providers have the potential to offer substitutes for landline local exchange service. However, presently there are technological, economic, and legal characteristics of CMRS that distinguish it from landline local exchange service and thus must be accounted for in the development of realistic regulatory policies:

(1) CMRS providers are exempt from the obligations, duties and requirements that apply to other local exchange carriers, including the following:

- The Omnibus Budget Reconciliation Act of 1993 preempts state and local governments from regulating the entry of or the rates charged by CMRS providers.[22] By contrast, local exchange

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[21] If the incumbent LECs are ignoring the FCC in this particular matter, there is reason to believe that they will similarly ignore the FCC's directives in other matters regarding the facilitation of entry by potential landline competitors. In the upcoming months, the Commission should bear in mind that mere satisfaction of a so-called "competitive checklist" by an incumbent LEC, though nominally responsive to the requirements of the Telecommunications Act, will not necessarily prevent anticompetitive behavior by incumbent LECs.

[22] Pub. L. No 103-66, Title VI, §6002(b), 107 Stat. 312 (1993) (codified at 47 U.S.C. §332(c)(3)(A)). The Act also states that "[n]othing in this subparagraph shall exempt providers of commercial mobile services where such services are a substitute (continued...)

carrier entry and rates are regulated by state public utility commissions.

- Furthermore, because CMRS providers are not affirmatively considered to be local exchange carriers, they are not subject to any of the duties that are expressly set forth for local exchange carriers in Section 251(b) (e.g., number portability, resale, etc.). By contrast, all local exchange carriers – including new, non-dominant CLECs – must offer "equal access" dialing parity.[23]

- The 1996 Act explicitly exempts CMRS providers from any obligation to provide toll dialing parity to non-affiliated interexchange carriers.[24]

- Finally, the 1996 Act explicitly renders moot the pending issue of equal access and would appear to permit the FCC to consider further the merits of resale obligations on CMRS providers.

(2) Second, the pricing and technical configurations of CMRS services that presently exist lead to traffic imbalances that suggest bill and keep is not an appropriate long-term model:

- As noted by the Commission, incumbent LECs typically terminate many more calls that originate from the cellular network than an interconnecting cellular network terminates LEC-originated calls.[25]

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[22](...continued)
for landline telephone exchange service for a substantial portion of the communications within such State." Id.

[23] 1996 Act at Sec. 251(b)(3).

[24] Id. at Sec. 705 (to be codified at 47 U.S.C. 332(c)).

[25] NPRM at para. 14. The FCC indicates that Pacific Telesis reports that 94% of LEC-CMRS exchange traffic terminates on its network and 6% of LEC-CMRS traffic terminates on wireless networks. Id. at para. 40 n.60. There are many probable reasons for this imbalance: Because cellular customers must pay for incoming calls, they tend not to publish, or even to divulge, their telephone numbers, and landline callers may be less likely to call cellular customers because users of cellular services "are on the move" and thus it is not necessarily known when they will be near their cellular phone.

- Because their customers are mobile, it is harder for cellular providers to locate them in order to terminate calls than it is for landline carriers to locate their customers, i.e., the incidence of non-revenue airtime for landline-cellular calls is greater than for cellular-landline traffic.
- It is too soon to predict the traffic flow (either volume or direction) for PCS providers.

The existence of these fundamental differences in the legal treatment of CMRS providers and local exchange carriers suggests that while some facilities-based competitive LECs may be able to "earn" co-carrier status by virtue of the enumerated regulatory constraints and duties imposed upon them by the 1996 Act, CMRS providers may never be able to achieve that status. In any event, as a long-term matter, the Commission should not bootstrap CMRS providers into an automatic entitlement to co-carrier status before these issues are resolved.

2. General Pricing Principles

Although the 1996 Act provides specific guidelines on how charges for transport and the termination of traffic should be determined, the Commission retains substantial discretion in applying these guidelines to CMRS-LEC interconnection charges. Section 252(d) of the 1996 Act indisputably applies to incumbent LEC-CLEC interconnections; however, one of the critical questions in this NPRM is whether this language applies (or should apply) to the establishment of CMRS-LEC interconnection rates. Indeed, in its Order and Supplemental Notice of Proposed Rulemaking released February 16, 1996, the Commission recognized this uncertainty in its statement that Sections 251 through 253 "may" affect proposals in the NPRM.[26]

The NRPM contemplates the potential for CMRS to substitute for landline service. In order for this long-term vision to be realized, it is essential that the rates for CMRS-LEC interconnection be set to allow economically efficient competition to emerge. One of the overriding goals in this and related FCC proceedings should be to ensure that basic monopoly unbundled elements are cost-based.[27] If essential network functions and features are priced too high, this will thwart competitive entry and the development of innovative telecommunications-based applications.

In order to establish cost-based rates, it is critical to examine the manner in which incumbent LECs allocate costs among their numerous services. Ultimately, the consequence of the misallocation of incumbent LEC costs would be to deny consumers reasonable rates for services in which the carriers retain substantial market power and to deprive consumers of a wide diversity of choices of potentially competitive telecommunications services. Therefore, cost studies should be

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[26] In re Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers, Order and Supplemental Notice of Proposed Rulemaking, CC Docket No. 95-186, FCC 96-61, para. 6 n.3. (February 16, 1996).

[27] The FCC is concerned that this approach could lead to "contentious, and time-consuming administrative proceedings to resolve the complex issues raised by cost studies." NPRM at para. 57.

fully documented, and allocations of overhead costs should be comprehensively justified and supported.[28]

a. Ramsey pricing is inappropriate for the establishment of incumbent LEC rates for interconnection.

The NPRM seeks comment on the use of Ramsey pricing in markets in which competition is developing.[29] Under Ramsey pricing, the size of "markups" over incremental cost are based upon the elasticity of the demand for services supplied in common. Ramsey pricing is inappropriate because it enables an incumbent LEC to shift costs associated with entry into new competitive markets over to the captive (inelastic) monopoly services.

To the extent that Ramsey pricing is applicable at all, its use must be limited solely to a purely monopolistic environment, i.e., one in which elasticities are not determined by the

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[28] The abysmal track record of incumbent LECs in this regard suggests that FCC oversight will be essential. See for example, the FCC's statement in one of its expanded interconnection orders, "[b]ased on our review of the LECs' direct cases and accompanying cost support data filed in response to the Phase I Designation Order, we conclude that most of the LECs have failed to meet their Section 204(a) burden of demonstrating that their overhead loading levels and, consequently, their virtual collection rates, are just and reasonable." In re Local Exchange Carriers' Rates, Terms, and Conditions for Expanded Interconnection Through Virtual Collocation for Special Access and Switched Transport, Report and Order, 10 FCC Rcd 6375, para. 2 (1995) (footnote omitted). See also Ameritech Operating Companies, et al., Order, 10 FCC Rcd 1960 (1995) in which the FCC states, "[t]hus, based on the current record, we conclude that in their tariff support materials, most LECs have failed to justify their proposals to recover a greater share of overhead costs in charges for expanded interconnection services than they recover in charges for comparable services." Id. at para. 24.

[29] NPRM at para. 51.

presence or absence of competitive alternatives. This is **not** the environment in which incumbent LECs are offering service, particularly as competition for local services becomes more prevalent. In the present environment, incumbent LECs are pursuing strategic capital investment programs intended to support and to facilitate their entry into new services and new markets. Furthermore, unlike the incumbent LECs, no competitive firm that sets all of its prices at incremental cost has any assurance of recovering its embedded costs elsewhere.

The fact that incumbent LECs are using substantial common plant and resources to support basic monopoly telephone services and new competitive ventures raises significant concerns about the manner in which the incumbent LECs propose to identify and allocate common or "group" costs in their cost studies. The 1996 Act prohibits cross-subsidization of a carrier's competitive services with its noncompetitive services, charging the FCC and state public utility commissions with establishing "any necessary cost allocation rules, accounting safeguards, and guidelines to ensure that services included in the definition of universal service bear no more than a reasonable share of the joint and common costs of facilities used to provide those services."[30]

Ideally, joint and common plant should be assigned to monopoly and competitive services based upon cost-causation principles, i.e., costs should be assigned on the basis of the purpose for which the costs were incurred. However, the mere use of a particular common resource to furnish a particular service would not justify the assignment of its costs unless it could be

[30] 1996 Act at Sec. 254(k).

shown that the resource was absolutely necessary as the economic choice for that service's provision. By contrast, Ramsey pricing would allow incumbent LECs excessive flexibility to recover the costs of common plant and resources from the least competitive, most monopolistic of its services, such as interconnection of competing networks. Designed for a monopoly environment, Ramsey pricing produces distorted results when some markets are competitive and others are not.

The basic theory of Ramsey pricing is that it minimizes economic distortions that might otherwise result from setting prices for individual services at levels removed from incremental cost. However, an economically neutral result will not be produced if Ramsey pricing is applied where competition is selectively present. Rather than minimize economic distortions, the targeted use of incremental cost pricing in only those markets in which some actual competition is present will serve only to weaken and possibly eradicate that competition. Incumbent LECs may seek to utilize Ramsey pricing as a convenient excuse for predation, and the fundamental flaw in that proposed pricing rationale should not escape the Commission's notice.

b. The FCC should reject the efficient component pricing rule

The NPRM also seeks comment on the use of the efficient component pricing rule ("ECPR") for markets in which competition is developing.[33] The ECPR holds that the price of any service element furnished by an incumbent LEC to a competitor should be equal to the incremental cost of providing the service plus any

[33] NPRM at para. 53.

foregone contribution that the LEC would suffer by virtue of "losing" the ultimate customer to the competitor. In markets that are only partially competitive, this "rule" is nothing more than a transparent effort to clothe fundamentally anticompetitive practices in some distorted view of economic theory.

In a competitive market, the profit generated by a sale to any given customer generally goes with the customer. If the customer buys from firm B rather than from firm A, then B, not A, gets the profit. Firm A (as well as firms C, D and E) all have an incentive to maintain their prices close to cost in order to remain competitive; hence, any "contribution" that a given firm might be able to generate will be primarily attributable to some aspect of its production process or the nature of its product that gives it some particular, if temporary, advantage.[34]

In the case of dominant local telephone monopolies with extensive market power, such contribution is not constrained by competitive market forces and can be retained indefinitely or, when competition does arrive in a particular segment, can be readily shifted to other services for which no competition is present. The efficient component pricing rule thus sanctions continued and permanent exploitation of any pocket of market power that an incumbent LEC can retain even after competition

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[34] For example, suppose that Firm A's unit cost for the product is $10, whereas Firm B can produce the same good for $8, because Firm B has adopted a more efficient production process. All other things being equal, Firm B will be able to generate an additional $2 of profit until other firms mimic Firm B's technology.

enters particular niches of its extensive market. It allows — indeed, even demands — that the incumbent LEC shift all so-called "contribution" (the incumbent LECs' common euphemism for "monopoly profit") generated from serving a particular customer or market segment to the noncompetitive interconnection elements that will be required by any new entrant in order to compete with the incumbent LECs.

c. <u>In those limited instances where bill and keep is inappropriate, the FCC should base rates for mutual compensation on long run incremental costs and not on embedded costs.</u>

Among the principles that should guide the Commission as it establishes rates for network interconnection are simplicity, fairness, and economic efficiency. As is discussed in more detail below, there are certain circumstances where a bill and keep approach satisfies these three criteria and thus should be adopted. Where the circumstances do not justify the use of bill and keep mutual compensation, the FCC should then turn to cost-based rates as it seeks to establish prices for incumbent LECs' services.

The FCC seeks comment on the use of forward-looking long run incremental costs ("LRIC") as the basis for setting interconnection rates, recognizing that LRIC will not recover historical embedded costs of the network or the interstate share of the costs assigned through Part 36 separations rules.[35] The use of LRIC is entirely appropriate in a competitive environment. There should be no entitlement to the recovery of historical embedded costs under a price cap nor in a competitive environment

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[35] <u>NPRM</u> at para. 48.

and, indeed, Section 252 of the 1996 Act specifically excludes the use of embedded costs ("determined without reference to a rate-of-return or other rate-based proceeding") in the setting of prices for unbundled rate elements.[36]

The NPRM also seeks comment on the use of a specified allocator for the assignment of shared costs and overheads among all services,[37] referring to the Virtual Collocation Orders in which incumbent LECs were not permitted to collect more for virtual collocation charges in the overhead loading factor than the incumbent LEC collected in its competing DS1 and DS3 services.[38] This general approach has substantial merit and TW Comm fully supports the FCC's critical comparison of the overhead assigned to interconnection rate elements with the overhead assigned to the incumbent LEC's own comparable competitive services.

Specifically, under conditions where a mutual compensation rate is desirable, LECs should be required to set the price for interconnection at a rate no higher than its incremental cost, including variable common costs.[39] While incumbent LECs often

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[36] 1996 Act at Sec. 252(d)(1).

[37] NPRM at para. 52.

[38] Id. (citing In re Local Exchange Carriers' Rates, Terms, and Conditions for Expanded Interconnection Through Virtual Collocation for Special Access and Switched Transport, Report and Order, 10 FCC Rcd 6375, para. 81 (1995)).

[39] With respect to interconnection rates (not mutual compensation), the Telecommunications Act allows for a "reasonable profit." See 1996 Act at Sec. 252(d)(1)(B). The FCC should apply this congressional guidance to the establishment of interconnection rates so as to allow a reasonable recovery of shared costs and variable overhead costs that are identifiable on a prospective basis.

portray "common costs" as being fixed, in reality they are entirely variable and volume-sensitive when considered on an aggregate basis, and may include "unassignable" costs arising from inefficient operating practices as well as costs associated with technologically and/or economically obsolete plant. Appendix A, a regression analysis of LEC accounting data relating overhead expenses to total direct (non-overhead) costs, derived from public FCC reports, confirms this fact.

Even though one cannot associate overhead costs directly with individual services, there is no question that overheads vary linearly and in proportion to those direct costs that can be specifically identified. Accordingly, it is both appropriate <u>and necessary</u> to consider such overheads as <u>variable costs</u> for inclusion in incremental cost studies. Indeed, to do otherwise would be knowingly and deliberately to <u>understate</u> incremental costs of individual services and service groups.

3. <u>Pricing Proposals (Interim, Long-Term, Symmetrical)</u>

a. <u>Bill and keep is the most appropriate interim model for mutual compensation between LECs and CMRS providers.</u>

The NPRM seeks an interim pricing approach that could be adopted and implemented "relatively quickly and with minimal burdens on CMRS providers, LECs, and regulators."[40] The Commission tentatively concludes that interconnection rates for local switching facilities and connections to end users should be priced on a bill and keep basis,[41] and also tentatively

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[40] <u>NPRM</u> at para. 59.

[41] <u>Id.</u> at paras. 25, 60.

concludes that rates for dedicated transmission facilities connecting LEC and CMRS networks should be based on existing access charges for transmission facilities.[42] TW Comm concurs with these conclusions, with the caveats discussed in these comments.

The FCC identifies the following advantages of bill and keep arrangements, and, based on these advantages tentatively concludes that a bill and keep arrangement for peak and off-peak periods is the best interim solution:

> (1) The arrangements are administratively simple and would not require the development of new billing or accounting systems.
>
> (2) The bill and keep model would prevent incumbent LECs with market power from charging exorbitant rates.
>
> (3) The bill and keep approach is economically efficient if either (1) traffic is balanced in each direction <u>or</u> (2) actual interconnection costs are so low that there is little difference between a cost-based rate and a "zero" rate.[43]

While the first two of these principles are clearly satisfied in the case of CMRS-LEC interconnection, traffic between CMRS providers and LECs is not remotely close to being balanced, and actual interconnection costs may not approximate zero.[44] Related to this question is an issue raised by the FCC, namely the merits of using a bill and keep approach solely for

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42 <u>Id.</u> at para. 3.

43 <u>Id.</u> at paras. 61-62.

44 In assessing costs of interconnection, it is essential to consider not only the costs of terminating traffic but also the costs of instituting systems to measure and bill for such traffic.